

# EXHIBIT 1

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

**FORM 10-Q**

☒ Quarterly Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended March 31, 2023

OR

☐ Transition Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission File Number: 1-11859

**PEGASYSTEMS INC.**

*(Exact name of Registrant as specified in its charter)*

Massachusetts

*(State or other jurisdiction of incorporation or organization)*

04-2787865

*(IRS Employer Identification No.)*

One Main Street, Cambridge, MA 02142

*(Address of principal executive offices, including zip code)*

(617) 374-9600

*(Registrant's telephone number, including area code)*

Securities registered pursuant to Section 12(b) of the Act:

<u>Title of each class</u>	<u>Trading symbol(s)</u>	<u>Name of each exchange on which registered</u>
Common Stock, \$.01 par value per share	PEGA	NASDAQ Global Select Market

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the Registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the Registrant was required to submit such files). Yes ☒ No ☐

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☒ Accelerated filer ☐ Non-accelerated filer ☐ Smaller reporting company ☐ Emerging growth company ☐

If an emerging growth company, indicate by check mark if the Registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

There were 82,961,204 shares of the Registrant's common stock, \$.01 par value per share, outstanding on April 19, 2023.

## PEGASYSTEMS INC.

## QUARTERLY REPORT ON FORM 10-Q

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**PEGASYSTEMS INC.**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)**

**NOTE 13. INCOME TAXES***Effective income tax rate*

	<b>Three Months Ended March 31,</b>	
	<b>2023</b>	<b>2022</b>
<i>(Dollars in thousands)</i>		
Provision for (benefit from) income taxes	\$ 5,249	\$ (7,683)
Effective income tax rate	(34)%	95 %

The effective income tax rate in the three months ended March 31, 2023 was impacted by the valuation allowance on the Company's U.S. and U.K. deferred tax assets and current taxes payable in the U.S. as a result of projecting taxable income that cannot be fully offset by net operating losses and available tax credits.

The Company recognizes deferred tax assets to the extent that it believes that these assets are more likely than not to be realized. Future realization of deferred tax assets ultimately depends on sufficient taxable income within the available carryback or carryforward periods. The Company's deferred tax valuation allowance requires significant judgment and uncertainties, including assumptions about future taxable income based on historical and projected information. On a quarterly basis, the Company reassesses the need for a valuation allowance on its existing net deferred tax assets by tax-paying jurisdiction, weighing positive and negative evidence to assess its recoverability. In making such a determination, the Company considers all available and objectively verifiable negative and positive evidence, including future reversals of existing taxable temporary differences, committed contractual backlog ("Backlog"), projected future taxable income inclusive of the impact of enacted legislation, tax-planning strategies, and results of recent operations. The weight given to the potential effect of negative and positive evidence is commensurate with the extent to which it can be objectively verified.

The Company intends to continue maintaining a full valuation allowance on the Company's U.S. and U.K. deferred tax assets until there is sufficient evidence to support the realization of these deferred tax assets.

**NOTE 14. (LOSS) PER SHARE**

Basic (loss) per share is calculated using the weighted-average number of common shares outstanding during the period. Diluted (loss) per share is calculated using the weighted-average number of common shares outstanding during the period, plus the dilutive effect of outstanding stock options, RSUs, and convertible senior notes.

Calculation of (loss) per share:

	<b>Three Months Ended March 31,</b>	
	<b>2023</b>	<b>2022</b>
<i>(in thousands, except per share amounts)</i>		
Net (loss)	\$ (20,774)	\$ (379)
Weighted-average common shares outstanding	82,604	81,680
<b>(Loss) per share, basic</b>	<b>\$ (0.25)</b>	<b>\$ -</b>
Net (loss)	\$ (20,774)	\$ (379)
Weighted-average common shares outstanding, assuming dilution <sup>(1)(2)(3)</sup>	82,604	81,680
<b>(Loss) per share, diluted</b>	<b>\$ (0.25)</b>	<b>\$ -</b>
Outstanding anti-dilutive stock options and RSUs <sup>(4)</sup>	1,348	4,178

(1) In periods of loss, all dilutive securities are excluded as their inclusion would be anti-dilutive.

(2) The shares underlying the conversion options in the Company's Notes are included using the if-converted method, if dilutive in the period. If the outstanding conversion options were fully exercised, the Company would issue approximately 4.2 million shares as of March 31, 2023.

(3) The Company's Capped Call Transactions represent the equivalent of approximately 4.2 million shares of the Company's common stock (representing the number of shares for which the Notes are initially convertible) as of March 31, 2023. The Capped Call Transactions are expected to reduce common stock dilution and/or offset any potential cash payments the Company must make, other than for principal and interest, upon conversion of the Notes, with such reduction and/or offset subject to a cap of \$196.44. The Capped Call Transactions are excluded from weighted-average common shares outstanding, assuming dilution, in all periods as their effect would be anti-dilutive.

(4) Outstanding stock options and RSUs that were anti-dilutive under the treasury stock method in the period were excluded from the computation of diluted (loss) per share. These awards may be dilutive in the future.

**NOTE 15. COMMITMENTS AND CONTINGENCIES***Commitments*

See "Note 7. Leases" for additional information.

**PEGASYSTEMS INC.**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)**

***Legal proceedings***

In addition to the matters below, the Company is or may become involved in a variety of claims, demands, suits, investigations, and proceedings that arise from time to time relating to matters incidental to the ordinary course of the Company's business, including actions concerning contracts, intellectual property, employment, benefits, and securities matters. Regardless of the outcome, legal disputes can have a material effect on the Company because of defense and settlement costs, diversion of management resources, and other factors.

In addition, as the Company is a party to ongoing litigation, it is at least reasonably possible that the Company's estimates will change in the near term, and the effect may be material.

The Company had no accrued losses for litigation as of March 31, 2023 and December 31, 2022.

***Appian Corp. v. Pegasystems Inc. & Youyong Zou***

As previously reported, the Company is a defendant in litigation brought by Appian in the Circuit Court of Fairfax County, Virginia (the "Court") titled Appian Corp. v. Pegasystems Inc. & Youyong Zou, No. 2020-07216 (Fairfax Cty. Ct.). On May 9, 2022, the jury rendered its verdict finding that the Company had misappropriated one or more of Appian's trade secrets, that the Company had violated the Virginia Computer Crimes Act, and that the trade secret misappropriation was willful and malicious. The jury awarded damages of \$2,036,860,045 for trade secret misappropriation and \$1.00 for violating the Virginia Computer Crimes Act. On September 15, 2022, the circuit court of Fairfax County entered judgment of \$2,060,479,287, consisting of the damages previously awarded by the jury plus attorneys' fees and costs, and stating that the judgment is subject to post-judgment interest at a rate of 6.0% per annum, from the date of the jury verdict (May 9, 2022) as to the amount of the jury verdict and from September 15, 2022 as to the amount of the award of attorneys' fees and costs. On September 15, 2022, the Company filed a notice of appeal from the judgment. On September 29, 2022, the circuit court of Fairfax County approved a \$25,000,000 letter of credit obtained by the Company to secure the judgment and entered an order suspending the judgment during the pendency of the Company's appeal. Appellate briefing is currently in process. Although it is not possible to predict timing, this appeals process could potentially take years to complete. The Company continues to believe that it did not misappropriate any alleged trade secrets and that its sales of the Company's products at issue were not caused by, or the result of, any alleged misappropriation of trade secrets. The Company is unable to reasonably estimate possible damages because of, among other things, uncertainty as to the outcome of appellate proceedings and/or any potential new trial resulting from the appellate proceedings.

***City of Fort Lauderdale Police and Firefighters' Retirement System, Individually and on Behalf of All Others Similarly Situated v. Pegasystems Inc., Alan Treffer, and Kenneth Stillwell***

On May 19, 2022, a lawsuit was filed against the Company, the Company's chief executive officer and the Company's chief operating and financial officer in the United States District Court for the Eastern District of Virginia Alexandria Division, captioned City of Fort Lauderdale Police and Firefighters' Retirement System, Individually and on Behalf of All Others Similarly Situated v. Pegasystems Inc., Alan Treffer, and Kenneth Stillwell (Case 1:22-cv-00578-LMB-IDD). The complaint generally alleges, among other things, that the defendants violated Section 10(b) of the Securities Exchange Act of 1934, as amended (the "Exchange Act") and Rule 10b-5 promulgated thereunder and that the individual defendants violated Section 20(a) of the Exchange Act, in each case by allegedly making materially false and/or misleading statements, as well as allegedly failing to disclose material adverse facts about the Company's business, operations, and prospects, which caused the Company's securities to trade at artificially inflated prices. The complaint seeks unspecified damages on behalf of a class of purchasers of the Company's securities between May 29, 2020 and May 9, 2022. The litigation has since been transferred to the United States District Court for the District of Massachusetts (Case 1:22-cv-11220-WGY), and lead plaintiff class representatives-Central Pennsylvania Teamsters Pension Fund - Defined Benefit Plan, Central Pennsylvania Teamsters Pension Fund - Retirement Income Plan 1987, and Construction Industry Laborers Pension Fund-have been appointed. On October 18, 2022, a consolidated amended complaint was filed that does not add any new parties or legal claims, is based upon the same general factual allegations as the original complaint, and now seeks unspecified damages on behalf of a class of purchasers of the Company's securities between June 16, 2020 and May 9, 2022. The Company moved to dismiss the consolidated amended complaint on December 19, 2022. The hearing on the motion to dismiss is scheduled for May 17, 2023. The Company believes the claims brought against the defendants are without merit and intends to defend against these claims vigorously. The Company is unable to reasonably estimate possible damages or a range of possible damages in this matter given the stage of the lawsuit, the Company's belief that the claims are without merit, and there being no specified quantum of damages sought in the complaint.

**PEGASYSTEMS INC.**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)**

*Mary Larkin, derivatively on behalf of nominal defendant Pegasystems Inc. v. Peter Gyenes, Richard Jones, Christopher Lafond, Dianne Ledingham, Sharon Rowlands, Alan Trefler, Larry Weber, and Kenneth Stillwell, defendants, and Pegasystems Inc., nominal defendant*

On November 21, 2022, a lawsuit was filed against the members of the Company's board of directors, the Company's chief operating and financial officer and the Company in the United States District Court for the District of Massachusetts, captioned *Mary Larkin, derivatively on behalf of nominal defendant Pegasystems Inc. v. Peter Gyenes, Richard Jones, Christopher Lafond, Dianne Ledingham, Sharon Rowlands, Alan Trefler, Larry Weber, and Kenneth Stillwell, defendants, and Pegasystems Inc., nominal defendant* (Case 1:22-cv-11985). The complaint generally alleges the defendants sold shares of the Company while in possession of material nonpublic information relating to (i) the litigation brought by Appian in the Circuit Court of Fairfax County, Virginia, described above, and (ii) alleged misconduct by Company employees alleged in that litigation. On January 10, 2023, the Court entered an order staying the matter until after a final judgment dismissing the *City of Fort Lauderdale* matter referenced above, the denial of a motion to dismiss in the *City of Fort Lauderdale* action, or if any related derivative complaint is filed and not stayed for the same or longer duration. The Company believes the claims brought against the defendants are without merit and intends to defend against these claims vigorously. The Company is unable to reasonably estimate possible damages or a range of possible damages in this matter given the stage of the lawsuit, the Company's belief that the claims are without merit, and there being no specified quantum of damages sought in the complaint.

*SEC Inquiry*

Beginning in March 2023, the U.S. Securities and Exchange Commission ("SEC") has requested certain information relating to, among other things, the accounting treatment of the Company's above-described litigation with Appian Corporation. The Company is fully cooperating with the SEC's requests.

## ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

### FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q (“Quarterly Report”) contains or incorporates forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995.

Words such as expects, anticipates, intends, plans, believes, will, could, should, estimates, may, targets, strategies, projects, forecasts, guidance, likely, and usually, or variations of such words and other similar expressions identify forward-looking statements, which are based on current expectations and assumptions.

Forward-looking statements deal with future events and are subject to risks and uncertainties that are difficult to predict, including, but not limited to:

- our future financial performance and business plans;
- the adequacy of our liquidity and capital resources;
- the continued payment of our quarterly dividends;
- the timing of revenue recognition;
- management of our transition to a more subscription-based business model;
- variation in demand for our products and services, including among clients in the public sector;
- reliance on key personnel;
- global economic and political conditions and uncertainty, including impacts from public health emergencies and the war in Ukraine;
- reliance on third-party service providers, including hosting providers;
- compliance with our debt obligations and covenants;
- the potential impact of our convertible senior notes and Capped Call Transactions;
- foreign currency exchange rates;
- the potential legal and financial liabilities and damage to our reputation due to cyber-attacks;
- security breaches and security flaws;
- our ability to protect our intellectual property rights, costs associated with defending such rights, intellectual property rights claims, and other related claims by third parties against us, including related costs, damages, and other relief that may be granted against us;
- our ongoing litigation with Appian Corp.;
- our client retention rate; and
- management of our growth.

These risks and others that may cause actual results to differ materially from those expressed in such forward-looking statements are described further in Part I of our Annual Report on Form 10-K for the year ended December 31, 2022, Part II of this Quarterly Report on Form 10-Q, and other filings we make with the U.S. Securities and Exchange Commission (“SEC”).

Except as required by applicable law, we do not undertake and expressly disclaim any obligation to update or revise these forward-looking statements publicly, whether due to new information, future events, or otherwise.

The forward-looking statements in this Quarterly Report represent our views as of April 26, 2023.

### BUSINESS OVERVIEW

We develop, market, license, host, and support enterprise software that helps organizations build agility into their business so they can adapt to change. Our powerful low-code platform for workflow automation and artificial intelligence-powered decisioning enables the world’s leading brands and government agencies to hyper-personalize customer experiences, streamline customer service, and automate mission-critical business processes and workflows. With Pega, our clients can leverage our intelligent technology and scalable architecture to accelerate their digital transformation. In addition, our client success teams, world-class partners, and clients leverage our Pega Express™ methodology to design and deploy mission-critical applications quickly and collaboratively.

Our target clients are Global 2000 organizations and government agencies that require solutions to distinguish themselves in the markets they serve. Our solutions achieve and facilitate differentiation by increasing business agility, driving growth, improving productivity, attracting and retaining customers, and reducing risk. Along with our partners, we deliver solutions tailored to the specific industry needs of our clients.

#### *Subscription transition*

We are transitioning our business to sell software primarily through subscription arrangements. Until we fully complete our subscription transition, which we expect will occur in 2023, our operating results may be impacted. Operating performance, revenue mix, and new arrangements in each period can fluctuate based on client preferences for our perpetual and subscription offerings. See the “Risk Factors” section of our Annual Report on Form 10-K for the year ended December 31, 2022 for additional information.